No. 18795

IN THE UNITED STATES COURT OF APPEAL

FOR THE NINTH CIRCUIT

-oOo-

SIDNEY MARTIN,

Appellant,

v

SAMUEL ROSENBAUM,

Appellee.

APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF CALIFORNIA,
CENTRAL DIVISION

APPELLANT'S BRIEF

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SIDNEY MARTIN,

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APPELLANT'S BRIEF

JURISDICTION

This is an appeal by Sidney Martin, individually, and doing business as Jersey Packing Company, a judgment creditor of the bankrupt (hereinafter referred to as Appellant), from an Order of the United States District Court for the Southern District of California, Central Division, dated and entered March 21, 1963.

affirming, on a Petition for Review, an Order of the Referee below permanently restraining Appellant from proceeding in an action captioned "SIDNEY MARTIN, ETC., Plaintiff, vs. SAMUEL E. ROSENBAUM, et al., Defendants, Docket No. 719 567, in the Superior Court of the State of California for the County of Los Angeles," and from in any manner enforcing or attempting to enforce any judgment which may have been entered therein.

This Court has jurisdiction of this appeal pursuant to 28 USC § 1291 and 11 USC § 47 (Bankruptcy Act of 1938, § 24).

STATEMENT OF THE PLEADINGS

These proceedings were initiated on November 8, 1961, when the bankrupt, SAMUEL ROSENBAUM (hereinafter referred to as Respondent) obtained an order requiring Appellant to show cause why Appellant should not be restrained from requiring the bankrupt to appear in supplementary proceedings then pending in the Superior Court, or from otherwise enforcing his judgment. [TR. 27][1] Appellant had previously obtained a judgment in the said Superior Court action and at the hearing on November 14, 1961,

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[1] TR 27 refers to transcript of record, Page 27. The symbol TR will hereinafter be used to designate the transcript of record.

the Referee below ruled that the judgment debt was dischargeable and that Appellant would be restrained. Appellant forthwith filed a Notice of Petition for Rehearing [TR. 33-37] with Points and Authorities. (Urging for the first time three additional grounds for denial of relief to Respondent, first, having allowed his default to be entered, Respondent had confirmed the truth of the allegations of the Complaint and that the judgment was conclusive on the character of the obligation and could not be re-examined; second, that Respondent to obtain relief must first have shown the Court that he had no adequate and speedy remedy in the State Court, and this he failed to do, and, third, that the Bankruptcy Court only could restrain a creditor where there was a showing that the bankrupt had no such adequate remedy in the State Court, and that at best, therefore, the Respondent should have been entitled to a stay, and not a permanent restraint, until such time as the Respondent moved to discharge Appellant's judgment pursuant to § 675(b) of the California Civil Code of Procedure.)

In response to said Petition for Rehearing [TR. 48-50], Respondent admitted that a default had been entered in the State Court action No. 719 567. [Paragraph 2, TR 48], and in a second separate defense pointed out, inter alia, that Appellant, because of filing a creditor's claim was bound

by the Bankruptcy Court's decision.

A hearing was held on the Petition for Rehearing on November 28, 1961. The Referee again ruled that the judgment debt was a dischargeable one. The Respondent's counsel submitted Findings of Fact and Conclusions of Law, objections were made thereto, and the Referee thereafter prepared his own Findings of Fact and Conclusions of Law [TR. 58-64], and ultimately made and entered an Order on March 12, 1962.

On March 20, 1962, Appellant filed a Petition for Review of the Referee's Order [TR. 65-71]. The Referee, on March 30, 1962, filed his Certificate on Petition for Review of the Referee's Order of March 12, 1962, [TR. 72-77], asserting that there were but two issues, first, whether the Court could receive extrinsic evidence, and, second, whether it had abused its discretion in not reopening the case for further evidence. After an extension, Points and Authorities were filed on behalf of the Appellant [TR. 79-80] and a detailed Memorandum was filed on April 24, 1962. [TR. 81-96] Respondent filed a Memorandum in Opposition thereto [TR. 97-104] on April 30, 1962, and the Petition for Review was set for hearing on September 10, 1962. [TR. 105]

The Petition was argued on September 10, 1962, but it was not until March 21, 1963, that Judge Hall entered

an Order affirming the Referee [TR. 106].

Appellant, on April 1, 1963, filed a motion for re-hearing on April 15, 1963. [TR. 107-111]. Said Motion was denied and this Appeal taken.

STATEMENT OF THE CASE

A. INTRODUCTION

Judge Hall, in his Order below, indicated that the Appellant had not seen fit to obtain a transcript to the testimony and stated that the only credible thing in that respect was the recital of facts contained in the Certificate of the Referee and the Findings of Fact. Judge Hall was not altogether correct. He should have added that the facts admitted in the Petitions and Responses filed by the parties obviously would be evidence. So would the documentary evidence. Moreover, there is a partial transcript of the Referee's statements which has been added to this record to indicate the difference between what the Referee said, and what he ultimately prepared in his Findings of Fact.

Basically, the Referee's Certificate sufficiently states the facts for the purpose of review and appeal so that a full transcript, other than the partial transcript,

was in the opinion of the Appellant's counsel, unnecessary. Most of the so-called testimony concerned the bankrupt's version of the facts alleged in the Complaint which, in Appellant's view, (otherwise set forth in this Brief), were immaterial since the principal point in this Brief is that the Referee's right to review the State Court record is a limited one, and that he cannot go beyond a Complaint and a Default which admits the facts and retry the facts and reach a different conclusion then that reached in the State Court.

The Court should also bear in mind that the testimony of the Respondent was taken subject to a motion to strike because, in line with the foregoing, Appellant contended that the Respondent was estopped to go beyond the Complaint, Default and Judgment entered thereon. [Partial Transcript, p. 2]

B. THE EVIDENCE PRESENTED

The Referee's transcript indicated that the evidence was presented by means of the pleadings, documentary evidence and testimony of the bankrupt. At the initial hearing on November 14, 1961, it was shown that on March 25, 1959, Appellant, a citizen of the State of New Jersey, had filed a Complaint in the Los Angeles Superior Court

[Exhibit "A" in evidence] seeking a Judgment on three common counts for $3,991.93 and, in the alternative, on a fourth count, for $3,990.50, charging that the Respondent had, upon false pretenses and fraudulent representations, purchased goods and credits when he knowingly and intentionally did not intend to pay for said goods. [Pages 3 and 4 of Exhibit "A"].

Respondent had been duly served with a copy of the said Summons and Complaint, and after failing to answer or otherwise plead, his default was entered. Appellant, following the Superior Court rule, then had submitted an Affidavit of Proof [Exhibit "B" in evidence] and a Judgment was entered in Department 63 by Commissioner Nichols. In support of this, the Appellant then asked the Court to refer to the Proof of Claim that had been filed in the Bankruptcy Court.

Appellant's counsel then indicated that the payments were thereafter made by bankrupt until bankrupt filed a voluntary petition in bankruptcy on January 24, 1961. [TR. 2, etc.]

It should be noted that Schedule "A"-3 [TR. 6] listed Appellant as a Judgment Creditor. The Appellant then asked the Court to refer to the Petition in Bankruptcy. Appellant had filed a Proof of Claim in this matter on June 21, 1961 [TR. 22] asserting that he held an unsecured

claim, which had been reduced to a Judgment for $3,990.50, plus interest and costs. The Proof of Claim recited as to the Judgment that there was a "certified copy annexed hereto and made a part hereof."

It must and should be noted that, at this initial hearing, the Referee made no comment or statement that the certified copy of the Judgment was not annexed to the said Proof of Claim.

(It was only at the re-hearing that the Referee stated that the Proof of Claim did not have a certified copy of the State Court Judgment.) [Referee's transcript of evidence, 7:9-25.] If the certified copy of the Judgment was not present, the only reference made to it was a nebulous suggestion to Appellant's counsel to "complete the record". [Referee's transcript of evidence, 8:15-23] It was only at the second hearing that Appellant's counsel informed the Referee that it was the first time that the Referee had indicated that a certified copy was not attached to the claim and the Appellant's counsel stated to the Referee that it was his understanding that when the Referee referred to completing the record, that what the Referee desired was the testimony of Mr. Rosenbaum, [the transcript of evidence, 9:24-26].

It must and should also be noted that the fourth count of the Complaint, the fraud count, was for $3,990.50, the

same amount referred to in the Proof of Claim, and a clear indication that the Judgment referred to in the Proof of Claim had reference to the fraud count, and not to the common counts. Moreover, the Referee should have known, or certainly should have taken judicial knowledge of the procedure in the State Court which required a proving up of a Judgment before a Referee only in a fraud count, and not for the common counts.

In summary, at the initial hearing on November 14, 1963, the Referee below considered only the Petition in Bankruptcy, Proof of Claim and the documentary evidence.

At the second hearing, in response to what he thought was the desire of the Referee to complete the record, Appellant's counsel, over objection, examined the Respondent as to the background of the Judgment, and the claim upon which it was based. The testimony of Respondent is set out in the Referee's Certificate. [TR. 75-76] In brief, the Respondent simply contradicted what he and his counsel believed to be the material allegations in the Affidavit of Proof. Respondent was well aware that the Appellant, then being in New Jersey, would not personally take the stand in rebuttal.

Despite the categorical denials, Respondent confirmed in his testimony that he had done business with the Appellant, that he was doing business with the discount

store in New Jersey known as "Two Guys from Harrison" and that once he started doing business with "Two Guys" (whether he conceded he was a concessionaire or not, the volume of his purchases doubled) [TR. 75] and that the Appellant's risk of doing business with Respondent was directly related to his relationship with "Two Guys". In his testimony, Respondent further mentioned that his payments from "Two Guys" were weekly. Although he denied the conversations set forth in Paragraph 4 of the Affidavit of Proof that his relationship with "Two Guys" was an opportunity of a lifetime, it is significant that the amount of $4,000.00 he allegedly collected just before he left New Jersey, was the approximate amount which was delivered to him from July 1st until July 12, 1958 (the payment of which would have accounted for the $4,000.00 referred to by the bankrupt). Apart from whether the Referee below should have taken evidence extrinsic to the record, the most that can be said of the Respondent's testimony is that he fairly related the situation, but where the facts would entail testimony of the Appellant and other witnesses, he simply denied such conversations.

C. FINDINGS OF FACT

After the rehearing on November 28th, the Referee

again indicated that he would hold in favor of the Respondent, and directed that findings of fact and conclusions of law be prepared. A draft of the proposed Findings of Fact was submitted, objections were made thereto, and finally, on March 12, 1962, the Referee prepared and filed his own Findings of Fact.

Generally, the Findings of Fact followed and confirmed the pleadings in bankruptcy, and were based on the Respondent's testimony. The Referee made little, if any, reference, however, to the documentary evidence and to the stipulated pleadings, and it is these points which Appellant challenges as erroneous for generally, there is no dispute as to the basic factual background of this case which is set forth in the Findings of Fact. In light of the emphasis apparently placed by the Referee and also the District Court Judge on the failure of the Appellant to attach a certified copy of the Judgment, we can only point out that the Referee found [Findings of Fact II] that the bankrupt had listed Appellant as a Judgment Creditor, that the Appellant had filed the Proof of Claim reciting that he was, in fact, a Judgment Creditor [Findings of Fact III], that the Estate had been closed on October 26, 1961. [Findings of Fact IV], that the Appellant had commenced proceedings to enforce his Judgment [Findings of Fact IV-1/2], and that the Appellant had

urged that his Judgment was a non-dischargeable one under § 17(a)2 of the Bankruptcy Act [Findings of Fact VI]. As we shall note, under the legal argument, our principal objection to the Findings of Fact are not what they state, but what they failed to state and, further, that the Referee made Findings on facts which should not have been considered by the Court.

Although we urged before the Referee and continue to urge that the Referee should not have taken extrinsic evidence, an example of the failure of the Findings of Fact to state the evidence can be found in the Referee's Certificate on Review with the Findings IX and X. The comparison will show that the Referee, although there was oral and documentary evidence, failed to indicate that the Respondent had more than doubled his business by reason of doing business with "Two Guys from Harrison", that the business relationship between Appellant and Respondent had changed, that the average amount of business after Respondent started doing business with "Two Guys" had more than doubled, that Respondent was or was not a concessionaire, that there is no finding one way or the other that the Respondent represented to Appellant that his position was improving, and that his relationship with "Two Guys" was or was not extremely satisfactory and was or was not his opportunity of a lifetime.

Additionally, the Findings of Fact are incomplete and, therefore, erroneous in that there are no findings on evidence presented to the effect that Appellant had filed an action in the Superior Court, No. LASC 719, 567, upon a Complaint alleging false pretenses, that the Respondent was duly served, that he defaulted, and that a Judgment was entered, and most importantly, that bankrupt took any steps or sought any remedy in the State Court prior to seeking relief before the Referee below.

STATEMENT OF POINTS ON WHICH APPELLANT INTENDS TO RELY ON APPEAL.

The points on which appellant intends to rely on appeal are:

1. In ascertaining whether a Judgment has been discharged in bankruptcy, may a Bankruptcy Court go behind the Judgment and receive extrinsic evidence for the purpose of determining the character of the debt upon which the Judgment is based.

2. To what extent can a Bankruptcy Court examine the record in the State Court and hear evidence extrinsic thereto where the State Court Judgment was entered by default and where the material allegations of the Complaint in the State Court sufficiently pleaded an intent to

defraud, and that the Bankrupt knowingly or fraudulently made materially false statements.

3. Is the Creditor's Judgment founded upon a liability which is non-dischargeable under the provisions of § 17(a)2 of the United States Bankrupt Act.

4. To what extent must the Bankrupt prove that he has no adequate or speedy remedy in the State Court in order to call upon the exercise of the jurisdiction of the Bankruptcy Court to restrain a creditor.

5. Will the supplementary proceedings enjoined by the Referee so interfere with the possession or custody of any property of the Bankrupt, or unduly impede or embarrass the Court in the administration of the Bankrupt's estate, or after acquired property, so that a permanent restraint is unnecessary.

6. Do adequate remedies, if any, exist in the State Court so that a permanent restraint is unnecessary.

7. Under what special circumstances should a Referee exercise his discretion in entering a permanent restraint against the creditor.

8. Must a Referee find special circumstances in order to exercise his discretion before entering either a temporary or permanent restraint against a creditor.

9. Was there an abuse of discretion on the part of the Referee in entering a permanent restraint against the creditor.

10. Did the Referee enter Findings of Fact and/or Conclusions of Law that were erroneous.

11. Did the Bankruptcy Court have jurisdiction over the person of this creditor to summarily proceed where the Referee apparently questioned the validity of the claim and found that no part of said Judgment, certified or otherwise, was attached to the said claim.

12. Did the Referee abuse his discretion in refusing to reopen the case, for further evidence.

13. Were the Findings of Fact incomplete and, therefore, erroneous in that there are no Findings on the evidence presented to the effect that petitioner had filed an action in the Superior Court, No. LA 719 567, upon a Complaint alleging false pretenses, that Bankrupt was duly served, that he defaulted, and that proof of such fraud was submitted by Affidavit to the Commissioner, who, thereupon, entered Judgment based upon said fraudulent allegations.

14. Were the Findings of Fact incomplete and also erroneous in that there was no finding that the bankrupt took any steps or sought any remedy in the State Court prior to seeking relief in the Bankruptcy Court.

15. Was Paragraph I of the Conclusions of Law incomplete and, therefore, erroneous in that there was no conclusion that the equity jurisdiction of the Court

could be exercised only in unusual circumstances and where a specific embarrassment arose.

16. Was Paragraph III of the Conclusions of Law incomplete and, therefore, erroneous for the reason that while the Court may go behind a Judgment under certain conditions, where the Judgment is based upon proper allegations of fraud and false pretenses following a default, the Findings of the State Court are conclusive upon those issues tendered and the Bankruptcy Court has no authority to go behind that Judgment.

17. Were Paragraphs V and VI of the Conclusions of Law incomplete and erroneous in that the power of the Bankruptcy Court to enjoin the State Court action is a limited one and is to be exercised only after the Bankrupt is shown that he does not have an adequate remedy in the State Court and where there is no adequate remedy, that the power is to be exercised only until there is such remedy and that there is a remedy in the State Court following a discharge not only by injunction, but also by Code provision which permits a Bankrupt to expunge a Judgment from the record by filing a petition indicating that the Judgment is a dischargeable one and that he, in fact, has been discharged in bankruptcy.

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SUMMARY OF ARGUMENT

In summary, it will be Appellant's position that although the Bankruptcy Court below is clothed with equity jurisdiction to determine whether a claim founded upon a Judgment should be within or excluded from the effect of a discharge, such jurisdiction has been held to be exercised only in unusual circumstances and where specific embarrassment arises, and that it is the duty of the party seeking such injunctive relief to first show the Court that such circumstances and embarrassment exist, and that here the bankrupt failed to show such circumstances.

Assuming that the Referee below properly exercised his jurisdiction, the second and most decisive point on appeal is that the Referee erred in taking and hearing evidence extrinsic to the Judgment by default which the Appellant had obtained in the Los Angeles Superior Court because a Judgment by default, similar to a Judgment by stipulation, admits the material allegations of the Complaint and is conclusive as to the issues tendered by the Complaint. While, in ascertaining whether a Judgment has been discharged in bankruptcy, broad language has stated that a Bankruptcy Court may go behind the Judgment to examine the entire record, and where the record before the

Bankruptcy Court is not complete or in doubt receive extrinsic evidence for the purpose of determining the character of the debt upon which the Judgment is based, this rule is limited by two conditions on its face: First, that the record before the Bankruptcy Court be incomplete, and second, that the record before the Bankruptcy Court be in doubt. Here the Referee's transcript shows that he considered the allegations of the Complaint (which had been admitted by the default) sufficient in themselves to constitute fraud, and a judgment thereon, a non-dischargeable one. But having done this, the Court completely ignored the established decisions as to the effect of the issues tendered by the Complaint and came to a different conclusion by doubts which he stated were raised by the Affidavit of Proof filed in the State Court. This is not the type of doubt which permits a Court to determine the character of the debt. The Referee then sought to justify his action by finding incompleteness in the absence of a certified copy of the Judgment which Appellant assumed to be annexed to the Proof of Claim.

Here, again, the transcript of evidence shows that Appellant had offered the Proof of Claim with what Appellant believed to be a certified copy of the Judgment annexed thereto as part of the Appellant's case. It was not until after the re-hearing that the Referee specifically

suggested by his statements that the record was not complete due to the absence of a certified copy of the Judgment annexed to the Proof of Claim.

As we shall hereafter show, the code and general orders do not require a certified copy of a Judgment to be annexed to a Complaint, and that the reference to a Judgment is sufficient proof that a Judgment existed. Apart from the Proof of Claim, the very Petition of the bankrupt was to restrain a Judgment, the response of the bankrupt to the Petition for a re-hearing admitted a default following the filing of the Complaint, and the Findings of Fact referred to a Judgment. Apart from the fact that the Proof of Claim recited the original Judgment being for the sum of $3,990.50 which was the same as the fourth count in the Complaint submitted to the Referee, if the Referee, to satisfy such doubts as may have existed, wanted to review a copy of the Judgment, the fair and proper procedure would be to suggest to Appellant's counsel that, for one reason or another, the certified copy of the Judgment which Appellant believed to be annexed to the Proof of Claim was absent. The transcript of evidence shows that the Appellant's counsel immediately sought to add a certified copy to the record when he learned of the absence of the certified copy of the Judgment, but the Referee refused to do so.

Apart from the cases which would indicate that, in this instance, a certified copy of the Judgment would be superfluous, if it was important, the Referee abused his discretion in refusing to reopen the case for the purpose of obtaining such a certified copy of the Judgment.

The third point in this Brief is that Appellant's judgment is a non-dischargeable one. Apart from the common counts, the fourth of the counts of the Complaint was one seeking damages for false and fraudulent representations which induced Appellant to sell goods on credit to the Respondent and for which he did not intend to pay. The Referee below conceded that the Complaint did allege fraud in terms that were non-dischargeable and when those allegations were admitted by the default of the defendant, it follows that certain Findings of Fact, not for what they said, but what they failed to say, were clearly erroneous.

Lastly, assuming that the Referee below was not estopped and could independently review the facts adversely to the Appellant, the proper course of procedure was for the Referee to grant only a temporary stay, until the Respondent could take advantage of the State Court remedies available to him to test the dischargeability or non-dischargeability of the defendant's Judgment.

ARGUMENT

I

THE REFEREE BELOW ERRED IN ENJOINING ENFORCEMENT OF APPELLANT'S JUDGMENT SINCE HE DID NOT FIRST FIND THAT THERE WERE UNUSUAL CIRCUMSTANCES OR SPECIFIC EMBARRASSMENT TO CALL UPON THE JURISDICTION OF A BANKRUPTCY COURT.

(a) A Bankruptcy Court has primary jurisdiction to determine the dischargeability of a debt. While the earlier cases question the authority of the Bankruptcy Court to determine the effect of a dischargeability of a judgment on after acquired assets, the Supreme Court in, Local Loan Company v Hunt, 292 U.S. 234, 54 S. Ct. 695, 78 Law. Ed. 1230, dispelled all doubts about the jurisdiction of the Bankruptcy Court to consider the question and it has been held that the Bankruptcy Court has both a primary and superior jurisdiction to determine the effect of its own decree of discharge, as the Referee has determined.

Holmes v Rowe, 97 F. 2d 537, 540 (C.C.A. 9, 1958)

However, jurisdiction aside, the proper inquiry in every case is whether that jurisdiction should be exercised. As was said in Local Loan Company, at 54 S. Ct. 698:

> "(The Court) probably would not and should not have done so except under unusual circumstances

Conclusion

I

[illegible]

such as here exist."

Thus, the Supreme Court properly pointed out that inquiry is not based alone on jurisdiction, but whether that jurisdiction should be exercised. In the Local Loan Company v Hunt case, only $300.00 was involved and the basis of dischargeability was a lien based upon an assignment of wages which was held to be insufficient and the Court's finding that the remedy in the State Court was entirely inadequate because it was wholly disproportionate to the trouble, embarrassment and possible loss of employment which was involved. It was thus the finding of this special embarrassment which supported the cases of Personal Industrial Loan Corp. v Forgay, 240 F. 2d 18, C.C.A. 10, 1957, and Seaboard Small Loan Corp. v Ottinger, 50 F. 2d 856, 859 (C.C.A. 4, 1931) which the Referee cited under the Conclusion of Law V. The essence of these cases, however, was a specific finding that the remedies in the State Court under the circumstances were entirely inadequate.

(b) There was no evidence nor finding that special circumstances existed for the exercise of the Court's jurisdiction. In his conclusions of law, [TR. 62-63] and specifically, conclusion of law No. IV, the Referee below found that he had the equitable jurisdiction to determine whether Appellant's claim was dischargeable, that the Court

[illegible]

Thus, the Supreme Court properly pointed out [illegible] equity, is not based alone on jurisdiction [illegible] but whether that jurisdiction should be exercised. In the Local [illegible] case [illegible] the [illegible] and a [illegible] upon an [illegible] and the Court [illegible] and [illegible] to the [illegible] possible loss of employment which was involved. It was [illegible] the [illegible] of this special [illegible] which supported the [illegible] Local Loan Co. v. [illegible] and [illegible] U.S. [illegible] the [illegible] under the [illegible] of the [illegible]. The [illegible] was a [illegible] that the [illegible] in the [illegible] Court [illegible] the [illegible] were [illegible].

(3) [illegible]

[illegible]

had primary and superior jurisdiction, and that exhaustion by the bankrupt of his State remedies was not a prerequisite to the exercise of the Court's injunctive power. With these conclusions, we have no argument. But what we do complain of is that there were no Findings of Fact and in no Conclusions of Law that the Respondent bankrupt did anything in the Court below to call upon the exercise of the Bankruptcy Court's jurisdiction. The only thing that the Respondent did was to allege in his Petition which supported the original Order to Show Cause to restrain Appellant [TR. 24], that he would be compelled to pursue along an expensive course of litigation in the State Court. At the hearing on November 14th, the Referee simply reviewed this Petition, the Response thereto, and ordered the Appellant to proceed with his case, assuming without argument, without evidence, without review of the procedures available in the State Court, that it had to exercise its jurisdiction.

In summary, we have reviewed every case cited by the Referee in his Conclusions of Law, and in none of them is the jurisdiction of the court exercised absolutely. Rather, the power of the court depends upon unusual circumstances and special embarrassment. Accordingly, in California State Board of Equalization v Coast Radio Products, 228 F. 2d 520 (C.C.A. 9, 1955), although it

was clear that the court had jurisdiction, it was held that such jurisdiction was permissive and should be exercised only in the sound discretion of the court and as a result the lower courts were reversed in seeking to force the Board of Equalization to file its otherwise non-dischargeable claim in the Bankruptcy Court and share in the assets of the Bankruptcy Court.

Apart from the other points, we submit that on this ground alone, the Referee below committed reversable error.

II

UNDER CALIFORNIA LAW, A JUDGMENT BY DEFAULT ENTERED IN THE STATE COURT IS CONCLUSIVE AS TO THE TRUTH OF THE FACTS ALLEGED IN THE COMPLAINT AND ALL FACTS NECESSARILY INCIDENT THERETO AND, THUS, THE REFEREE BELOW COMMITTED REVERSIBLE ERROR IN RE-TRYING THE ISSUES TENDERED BY THE COMPLAINT IN REACHING A CONTRARY CONCLUSION.

(a) A Judgment by Default admits the material allegations of the Complaint.

§ 462 of the Code of Civil Procedure provides that every material allegation of a complaint not controverted by the answer must for the purpose of the action be taken as true.

Crespi & Co. v Giffen, 132 CA 526, 530 (1933)

A material allegation in a pleading is one essential to the claim or defense, and which could not be stricken from the pleading without leaving it insufficient.

C.C.P. § 463.

Likewise, it has been held by the California courts for countless years that by permitting his default to be entered, a litigant confesses the truth of all the material allegations in the complaint.

Fitzgerald v Herzer, 78 Cal App 2d 127, 131 (1947).

In that case a judgment had been entered in a personal

injury action in which the acts of the bankrupt defendant were charged in the original complaint to have been grossly careless, reckless, negligent and wanton. The defendant received a discharge there on April 12, 1945, and thereafter the plaintiff brought an action on the judgment seeking a new judgment for the amount thereof with interest. The discharge was noted by the court and a judgment in favor of the defendant was entered. On appeal this was reversed. The court cited § 17 of the Bankruptcy Act and stated, at Page 130:

> "Whether a judgment is cancelled by a discharge in bankruptcy depends on the nature and character of the liability for which it was recovered. Therefore, in ascertaining whether the judgment upon which the instant action is based was discharged, the court will go behind the judgment, examine the entire record, and determine therefrom the nature of the original liability, and when necessary extrinsic evidence will be received for the purpose of determining the character of the debt. *(cases cited)"

At page 131 the court continued:

> "The acts of defendant were charged in the original complaint to have been grossly careless, reckless, negligent and wanton. To avoid a discharge in bankruptcy it was not necessary that the words 'willful and malicious' be used. The terminology in the

> complaint is the equivalent of 'willful and malicious' as used in the Bankruptcy Act."

Continuing further on the effect of the default judgment, the court stated, at page 130:

> "Since the judgment in the former action had become final, the court erred, not in rejecting plaintiff's offer of proof, for such proof was unessential, but in rendering judgment in favor of defendant on the evidence before the court, consisting of the complaint in the original action, the default of defendant and the judgment for plaintiff. The evidence tendered by the offer of proof would have established nothing more than defendant had admitted by his failure to answer in the first action. By permitting his default to be entered he confessed the truth of all the material allegations in the complaint (Wilshire Mortgage Corp. v O.A. Graybeal, 41 Cal. App. 1, 5 *; Strong v Shatto, 201 Cal. 555, 558 *; Brown v Brown, 170 Cal. 1, 5*) including the allegations of wantoness, recklessness and gross carelessness. (Van Epps v Aufdenkamp, supra 138 Cal. App. 622, 623 *)."

The gist of this ruling is found in the words following that quotation as follows:

> "A judgment by default is as conclusive as to the issues tendered by the complaint as

> if it had been rendered after answer filed and trial had on allegations denied by the answer. (Maddux v County Bank, 129 Cal. 665, 667; Morenhut v Higuera, 32 Cal. 289, 295) Such a judgment is res judicata as to all issues aptly pleaded in the complaint and defendant is estopped from denying in a subsequent action any allegations contained in the former complaint. (Horton v Horton, 18 Cal. 2d 579, 585; Harvey v Griffiths, 133 Cal. App. 17, 22). Since the only defense presented in the instance action was the discharge in bankruptcy, futile insofar as plaintiff's claim is concerned, judgment should have been rendered in favor of plaintiff on the evidence introduced." (Emphasis added)

In Van Epps v Aufdenkamp, 138 Cal. App. 622, 646, the Court stated as to the default of a bankrupt in a State Court action in the following language:

> "The respondent in the case now before us did not see fit to interpose a defense to the action, thereby admitting that while in possession of the certificates of stock, he unlawfully converted and disposed of the stock to his own use, to the damage of the plaintiff in the sum of $1,700.00. In line with Smith v Ladrie, supra, we are of the opinion that such conversion was willful, because it was voluntary, and malicious

[illegible]

if it had been rendered after expen- [illegible] during an [illegible] caused by the accident. [illegible]

[illegible]

In [illegible]

[illegible]

> because it was intentional, and that the judgment based upon such injury is not released by the discharge in bankruptcy."

While a default judgment, as stated in the case of Maddux v County Bank, 129 Cal. 665, 667, (1900) is not conclusive as to all matters, it is conclusive as to the truth of the facts alleged in the Complaint and all facts necessarily incident to such facts and to the enforcement of the claim therein set forth. For our purposes, the character of the obligation is based upon the facts as they existed at the time the Complaint was filed, and the facts at the inception of the debt alleged in the Complaint. It is conceded that the dischargeability of the debt upon the grounds of false representations must show that the false representations existed at the inception of the debt. Here, we submit the allegations of the Complaint (Exhibit "A" in evidence) clearly indicate fraud from the inception of the debt and a misrepresentation in the intention of the purchase of goods. See 2 Collier, 1630, § 17.16. The Bankruptcy Court's right to take extrinsic evidence is limited.

Our grievance with the Referee is not in the general law which he sets forth in Conclusions of Law I, II and III, but in his application of those rules.

It has long been held that the dischargeability of a

judgment is determined by the nature of the underlying claim. Boynton v Ball, 121 US 457, 7 S. Court 981, 30 Law Ed. 985. Where the claim is one for conversion, such as in Van Epps v Aufdenkamp, supra, or in Wilson v Walters, 19 Cal 2d 111, (1941), and a Judgment is obtained, there has been no problem. The Court simply looks beyond the Judgment, notes that the claim is one which is non-dischargeable, and excepts the Judgment from the discharge. Where the Judgment is based upon a note or claim, that Judgment would normally be dischargeable unless it could be shown that the note or claim was actually based upon false and fraudulent representations. Whether a Court can redetermine the dischargeability of the Judgment, in ascertaining whether in fact the note or claim was founded upon fraud, has divided the Courts. Fidelity and Casualty Company v Golombosky, 133 Conn. 317, 50 Atl. 2d 817 (1946) cited under Conclusions of Law I by the Referee, supports the minority position. In such cases, the Bankruptcy Court or the State Court has gone beyond the Complaint and ascertained the basis of the claim. California had adopted this minority position as set forth in US Credit Bureau v Manning, 147 Cal. App 2d 558 (1957) and Yarus v Yarus, 178 Cal App 2d 190 (1960), both cited by the Referee under Conclusions of Law III [TR 62]. For a complete discussion of this problem, see the annotation in

170 ALR 361. In re Tamburo, 82 Fed. Supp. 995, (DC Maryland, M.D., (1946)) cited by the Referee in Conclusion of Law IV, is one of those cases that stands for the proposition that the character of the debt is to be determined from the record of the proceedings in the Court which entered the Judgment.

Thus, if this was the case where the Judgment had been entered simply on the common counts or upon a Promissory Note without any reference to fraud, California following the minority rule, we could not object to the Referee's taking of extrinsic evidence to determine the nature of the underlying obligation.

However, in the instant case, where the Complaint alleges fraud, and sufficiently alleges fraud in the inception as the Referee himself conceded when at Page 6, lines 16 and 17 of the transcript of evidence, he stated:

> "While the Complaint in this case I think would be sufficient of itself."

and by reason of the default there is a stipulation admitting the material facts of that Complaint, the Judgment is one in fraud, is non-dischargeable and, thus, no extrinsic evidence can be taken.

In summary, the proper inquiry in any case is not the taking of extrinsic evidence, but whether the material allegations of the Complaint in the event of a stipulation or default

or proof during a trial, will or will not support the creditor's claims concerning the non-dischargeability of his Judgment.

If the material allegations, or the evidence, which are well-pleaded, or which are presented, support the creditor's position, there is no need for extrinsic evidence. If the material allegations do not support the creditor's claims that the Judgment is a non-dischargeable one, then under the Manning and Yarus cases, the creditor is given the opportunity of producing such extrinsic evidence. Conclusion of Law III cited by the Referee, upon which the Referee based his authority to retry the facts of this case, incorporates a condition precedent "when necessary". It must follow, therefore, that the Referee cannot in every case take extrinsic evidence because, otherwise, a condition precedent "when necessary" would be superflous. This Court should bear in mind that the general rule of a pre-Bankruptcy Judgment is that the validity and amount of it are res judicata. Pepper v Litton, 308 US 295, 60 S. Ct. 238, 84 Law Ed. 281 (1939). The history of the conclusiveness of Judgments in Bankruptcy, is traced in 3 Collier on Bankruptcy 1833, ¶ 63.11. Briefly, under the Act of 1867, because of full faith in credit, it was held that a Judgment of a State Court could not be impeached when presented as a claim in

Bankruptcy. Campbell's case, Fed Case 2, 349 (DC, PA). However, under present law, such a Judgment is held to be subject to collateral attack for lack of jurisdiction, Matter of Nelson, 36 Fed 2d 939 (DC Idaho) or for extrinsic fraud or collusion. But it has been held that a Judgment rendered by default conclusively establishes the creditor's claim and can be eliminated only by opening the default in the State Court. Matter of Smith, 36 Fed 2d 697, (CCA 2d).

As stated in Hendler v Walker, 200 Fed 566, (CCA Mo. 1912), the Court said:

> "The controlling question is whether the Judgment of the State Court concludes the controversy and bans the further prosecution of the claim in the Court of Bankruptcy. We think it does." * The Judgment was upon the merits." "The rule as to the conclusiveness of an adjudication when the same matter again comes up between the same parties is too familiar to require much restatement. It covers questions of both law and fact upon which their rights depend and those which might have been determined, as well as those which were."

(b) The Creditor's Judgment, being in fraud, is a non-dischargeable one.

Where a complaint seeks damages for false and fraudulent representations, and a judgment is entered in accordance

with the allegations of the complaint, that judgment even though a remedy for contract also existed, is not dischargeable by bankruptcy.

Wilson v Walters, 19 Cal. 2d 111, (1941);

In the Wilson case, plaintiff, a judgment creditor, sought a garnishment upon the salary of a public officer. Two grounds were raised. One, that public salaries were immune from garnishment, which ground was overruled. Second, that the judgment had been discharged by defendant's discharge in bankruptcy. This defense was also overruled, but the trial court was reversed with an order directing the disbursement of the funds to the judgment creditor.

As to the discharge in bankruptcy the Court there pointed out that the record showed a complaint in several counts, one being for money had and received, and one for damages for false and fraudulent representations made with the intent to deceive and upon which the plaintiff had acted and had been induced to advance money. The Court stated that it was apparent that all of the counts involved the same transaction and same money, and stated that the pleading of the actual fraud was complete and sufficient.

The defendant there had filed an answer denying the allegations of fraud, but after it was filed he stipulated that a judgment might be taken against him "in accordance with the allegations of the complaint herein".

The court cited the usual rules that it was immaterial whether or not plaintiff proved her claim in the bankruptcy proceedings, or that a judgment had been obtained, stating at Page 121:

> "The sole test of whether or not a liability is discharged in bankruptcy is not whether the claim is susceptible of proof in the bankruptcy proceedings under the bankruptcy laws. If a claim is not provable then for that reason alone, it is not discharged by bankruptcy. But in addition thereto a claim or liability which falls within the class expressly excepted by the bankruptcy act "from the discharge, is not discharged even though it is a provable claim."
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> * * * * * *
>
> "It cannot be said that plaintiff waived the tort, the claim based upon fraudulent representations, and relied upon contract in her action and is thereby foreclosed from asserting that her claim is based on fraud and not discharged in bankruptcy. The designation of her complaint at the beginning thereof as being for damages and breach of contract is of no significance. She stated counts both in contract and fraud, the stipulation for judgment and the judgment recited that the latter was in accordance with the allegations of the complaint. Therefore, it cannot be said that the Judgment is not

predicated on fraud, or that the liability on that basis was abandoned."

See also Crespi & Co. v Giffen, Supra, at Page 530.

(c) It was not necessary to annex a certified copy of the Judgment.

The Referee below indicated that the failure of the Appellant to annex a certified copy of the Judgment to his Proof of Claim filed in Bankruptcy was a decisive fact in creating "doubt" concerning the dischargeability of the Judgment. In fact, the refusal of the Referee to permit Appellant to file such a certified copy, was considered by the Referee to be one of the two principal issues in his Certificate of Review. [TR 74]

The fallacy of the Referee lies both in fact and in law.

(i) FACT

As a matter of fact, there is no question that Appellant had a Judgment by Default. For example:

(1) Appellant was listed as a creditor holding a Judgment in the bankrupt's Schedule "A-3" [TR 6];

(2) The very Petition which initiated this restraint alleged in Paragraph III thereof that Appellant was a Judgment Creditor [TR 23];

(3) The Proof of Claim filed by Appellant alleged that he was a Judgment Creditor. [TR 22];

(4) The Response of Respondent to a Petition for Rehearing before the Referee specifically admitted that a default was entered in the Superior Court action [TR 48];

(5) Finding of Fact IV-1/2 finds that Appellant commenced proceedings in "said Superior Court action for the purpose of attempting to enforce the Judgment entered therein". [TR 59];

(6) Finding of Fact VI makes reference to a Judgment [TR 60].

Is there any question that Appellant had a Judgment?

(ii) LAW

As to the law, the requirements for filing a Proof of Claim in Bankruptcy are set forth in § 57 of The Bankruptcy Act, 11 USC § 93 and General Order 21. Generally, a Proof of Claim consists of a statement under oath in writing signed by the creditor setting forth the claim, the consideration therefor, any securities held, payments made thereon, and that the claim is justly due and owing.

Certain claims, if founded on a written instrument,

are supposed to have the written instrument attached. 11 USC 93(b). General Order 21, however, in setting forth the written instruments to be attached, specifically does not include a Judgment, or a certified copy of a Judgment.

More importantly, as amended in 1960, 11 USC § 93 (a), provides that a Proof of Claim filed in accordance with the Bankruptcy Act, the General Orders and the official forms, even if unverified, shall constitute prima facie evidence of the validity and amount of the claim. Examination of Appellant's Proof of Claim [TR 22] shows full compliance with the Bankruptcy Act, the General Orders and the use of the official form, except perhaps in actually annexing a certified copy of the Judgment.

While not necessarily binding upon the Referee, no objections were made to Appellant's Proof of Claim during the pendency of the Estate. Moreover, after an Estate is closed, 2 Remington on Bankruptcy (Rev.) 498, § 1041, states that once an Estate is closed, the allowance or disallowance of a claim should not be considered or reconsidered. Further as to Judgments, 2 Remington 153, § 730, provides:

> "When a claim is based on a Judgment, a certified copy or transcript of the Judgment probably should be attached to the Proof of Claim to clarify the statement

of it, though it is doubtful whether a Judgment is within the intendment of the 'written instrument vision of the statute' (emphasis added)"

"Cox v Farley, 2 Ohio DEC. Reprints, 291, 2 West LM 315: "A record is undoubtedly the evidence of an indebtedness; but is it a 'written instrument?'* Now, from the use of the words 'written instument' it is clear that the code refers to an instrument executed by or between parties. Webster defines the word, as a writing containing the terms of the contract. In this sense, a record is not a written instrument. The Judgment of the Court is the ground of the action and the record is mere evidence of that recovery. The record is as accessible to the one party as to the other. It is public property and either party can obtain a copy of it." (Emphasis added.)

2 Remington 152, § 30 further states as to written instruments:

"Failure to file the instrument does not invalidate the claim, or raise any presumption against existence of a pertinent writing, the statute, and the direction on the official form to attach notes or negotiable instruments to the proof, being considered directory rather than mandatory". (Emphasis added)

See In Re Petrich, 43 Fed 2d 435 (DC Cal. 1930).

(d) If the Referee below considered the certified copy of the Judgment to be important, then the Referee should have permitted the claim to be amended upon the first request therefor.

The duty of a Referee to reconsider and amend Orders is governed under Federal Rules of Civil Procedure, § 60. Proofs of Claim are said to be amendable, not by reason of any provision of the Bankruptcy Act or General Orders, but because of the liberality in allowing amendments under Rules of Civil Procedure, § 15.

2 Remington, 176, § 746. Although the permission of a particular amendment lies in the Referee's discretion, it has long been the practice to permit amendments curing mistakes of either fact or law in the absence of fraud, provided injury to others will not result.

2 Remington 178, § 752, in cases cited in the footnote.

Thus, an amendment would be allowed to correct a technical defect in an affidavit which constitutes a formal proof of claim.

Re Supreme Appliance & Heating Co., 100 Fed 2d 200 (DC. Ky, 1951)

Recently it was held that since the Bankruptcy Court is a Court of Equity, the trend is toward greater liberality

in the allowance of admendments or amending of Proofs of Claim where there is anything in the record to justify such a cause of action.

Federal & Deposit Co. v Fitzgerald, 272 Fed 2d 121 (CCA 10,Colorado, 1959), Cert. Den., 362 US 919, 80 Sup. Ct. 669, 4 Law Ed. 2d 738.

Where the claim was based on a written instrument which was not submitted with the Proof of Claim it may be added by amendment even after the time to file a Proof of Claim has expired.

Globe Indem. Co. v Keeble, 20 Fed 2d 84 (1927 CCA 4)

In fact, a claim has been permitted to be filed wherein it appeared that the attorney who was supposed to file the Proof of Claim inadvertently forgot to file the entire Proof of Claim.

In re Oscillation Therapy Products, Inc., 94 Fed Supp 779 (DC New York 1951).

It irresistably follows that there is no foundation, either in law or fact, for the Referee's emphasis upon the lack of a certified copy of the Judgment, and his failure to permit a certified copy of the Judgment to be filed.

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III

CERTAIN FINDINGS OF FACT AND CONCLUSIONS OF LAW WERE CLEARLY ERRONEOUS, SHOULD BE SET ASIDE, AND CONSTITUTE REVERSIBLE ERROR.

Under Federal Rule of Civil Procedure 52, a finding of fact will be set aside if it is clearly erroneous as, for example, in not being supported by the evidence.

Campana Corp. v Harrison, 114 Fed. 2d 400 (C.C.A. 7, 1940)

In reviewing the conclusions of law, however, appellate courts have greater latitude and need not respect those conclusions that do not rest properly on the facts so found.

Bullen v De Bretteville, 239 Fed. 2d 824 (C.C.A. 9, 1956).

Under California law, the tests of which we believe are applicable here, findings must be made upon every material issue supported by substantial evidence.

Edgar v Hitch, 46 Cal. 2d 309 (1956).

Likewise, where affirmative matters are raised, findings must be made upon them.

See Bertone v City and County of San Francisco, 111 Cal. App. 2d 579 (1952).

Although findings can be implied, an omitted finding on a material issue is said to be fatal to the judgment.

See Zeller v Browne, 143 Cal. App. 2d 191 (1956).

The findings of fact which have been objected to are discussed at length above. Again, the principal vice of the Referee below is not in the particular findings that he did make, in general, but in his failure to make findings upon material matters which were submitted to him and his interpretation of the evidence which was presented to him.

We submit that where there are no findings on material issues, such failure is clearly erroneous, and where the omitted findings are pertinent to the decision of the Court, the fact of omission constitutes reversible error.

There is no presumption of correctness, however, as to a question or conclusion of law.

In re Newcomb Interests, Inc., 171 Fed. Sup. 704 (ND Cal. 1959) Affirmed Sub. Nom. Huffman v Farros, 275 Fed. 2d 350 (C.C.A. 9, 1960) (The issue there was the validity of a lease re-transfer agreement under California Law)

Whether the default judgment, under the doctrine of Fitzgerald v Herzer, Supra, is res judicata of the issue of fraud is, we submit, a question of law.

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IV

ADEQUATE REMEDIES EXISTED IN THE STATE COURT TO DETERMINE THE DISCHARGEABILITY OF A DEBT AND, AT BEST, A PERMANENT RESTRAINT WAS UNNECESSARY.

The Referee's Order [TR 63-64] permanently restrained Appellant from proceeding in the State Court action. Even if the Court properly exercised its jurisdiction and probably could take extrinsic evidence and redetermine the material allegations of the Complaint, we submit that the Court should not have permanently restrained the Appellant. The action that initiated these proceedings was an application for supplementary proceedings in the State Court. As to such supplementary proceedings, a motion could have been made in the State Court testing the dischargeability of the Judgment and, secondly, after one year under the provisions of Civil Code of Procedure, § 675 (b), the Respondent could seek to expunge the Judgment from the records upon the ground that it had been discharged in bankruptcy.

Normally, the Court in which a debt is proceeded upon is the proper forum to determine whether a discharge releases that particular debt.

Matter of Andrews, 47 Fed. 2d 949 (DC Cal. 1931). In the Andrews case, a creditor sought to bar the discharge of

the bankrupt, upon the ground that the only debt scheduled by the bankrupt was a non-dischargeable one. Although the bankrupt's discharge was granted, the Court stated that the proper forum for determining whether the debt was dischargeable or non-dischargeable was the State Court.

It has been further stated that an injunction should only be granted until the bankrupt can move in the State Court for a discharge, or the equivalent of a discharge.

Matter of Stoller, 25 Fed. Sup. 226. Thus, where there is a proper remedy, the matter should have been left to the State Court since the jurisdiction of the Bankruptcy Court while primary, is exceedingly narrow.

Ciaverelli v Salituri, 153 Fed. 2d 343 (1946).

In the latter case, the stay was vacated.

While it appears that the bankrupt may not have tested the dischargeability of the debt under § 675(b) for a year after his discharge in bankruptcy, the application for supplementary proceedings, we submit, was not such an overt act which would embarrass the bankrupt or cause him any great expense, and all other issues aside, the order of the Bankruptcy Court should have been

the State Court to initially allege that the underlying debt sounded in fraud. Rules of law are not always to be generalized; however, the error of the Referee below was in applying a Rule of Law to a factual situation not designed for that Rule of Law.

Under all the circumstances, therefore, we urge that the Findings of Fact and Conclusions of Law are clearly erroneous, and that, not only should the Referee and the District Court be reversed, but that this Appellate Court should rule that Appellant's Judgment was, in fact, a non-dischargeable one.

Respectfully submitted,

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C E R T I F I C A T E

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit and that in my opinion, the foregoing brief is in full compliance with those Rules.

Robert G. Leff